Before the
Federal Communications Commission
Washington, DC 20554

In the Matter of Application by Verizon Maryland Inc., Verizon Washington D.C. Inc., and Verizon West Virginia Inc., et al., for Authorization To Provide In-Region, InterLATA Services in Maryland, Washington, D.C., and West Virginia	)	WC Docket No. 02-384

DECLARATION OF MICHAEL LIEBERMAN
ON BEHALF OF AT&T CORP.

I. QUALIFICATIONS AND SUMMARY

1. My name is Michael Lieberman. I am District Manager in AT&T's Law and Government Affairs organization. In this position I am responsible for providing financial and industry analytical support for the costing and pricing of local telecommunications services. I was AT&T's primary participant in the development of the HAI/Hatfield Model of forward looking economic costs for local exchange networks and services, and I have been responsible for evaluating other costing models and methodologies such as the BCPM and the FCC's Synthesis Model. I have a Bachelor's degree in mathematics and a Master's degree in statistics from the State University of New York at Stony Brook. Before joining AT&T as a statistical consultant in 1978, I was a bio-statistical consultant with Carter-Wallace of Cranbury, New Jersey.

2. The purpose of this declaration is to explain why Verizon's switching rates in West Virginia should not be approved on the theory that they satisfy a benchmark comparison with

Verizon's switching rates in New York. Verizon's switching rates in West Virginia are 30 percent higher than the corresponding Verizon rates in New York on a cost adjusted basis. This fact cannot legitimately be overcome by rate-to-cost relationship of Verizon's *aggregate* non-loop rates in the two states. The Commission's method for comparing the aggregate non-loop rates between New York and other states is tainted by the pronounced tendency of the transport (interoffice) cost module of the FCC Synthesis Model to overstate the costs of unbundled transport, and to overstate those cost most greatly in the states with the lowest density of lines.

3. This phenomenon is far more severe in West Virginia than in any other state in Verizon's territory. On a cost-adjusted basis, Verizon's switching rates (or, more precisely, its weighted average rates for all non-loop UNEs other than transport) in West Virginia exceed their counterparts in New York by $1.79 per subscriber per month, or approximately 30 percent.

II. VERIZON'S SWITCHING RATES IN WEST VIRGINIA CANNOT BE UPHELD ON THE BASIS OF BENCHMARK COMPARISONS WITH NEW YORK.

4. It is my understanding that the Commission may not approve Verizon's 271 application without a specific finding that Verizon's non-loop and switching rates are TELRIC compliant. Section 271 (d)(3)(A) permits Verizon to begin providing in-region interLATA service only if the Commission finds that the company has satisfied the competitive checklist set forth in Section 271 (c)(2)(B). One of the items on the competitive checklist, found in Section 271 (c)(2)(B)(ii), mandates that the company seeking approval provide "[n]ondiscriminatory access to network elements in accordance with the requirements of sections 251(c)(3) and 252(d)(1). This latter section, I understand, requires that the price Verizon charges for a network element must be "based on the cost . . . of providing . . . *the* network element." 47 U.S.C. § 252(d)(1)(emphasis added).

5. In the past, however, the Commission has declined to examine the specific costs of providing individual network elements, and has instead relied on a benchmarking policy. Under this benchmarking policy, which I understand is essentially a shortcut for determining whether Verizon's rates are TELRIC compliant, the Commission has found that a Bell Operating Company's rates are TELRIC compliant if (a) the same carrier's prices for network elements have been examined and found to comply with TELRIC in another state, and (b) the rate-to-cost ratios of the carrier's prices in the state at issue do not exceed the corresponding ratios in the state where the Commission has already made a direct determination of the carrier's costs. To accomplish this, the Commission uses runs of the Synthesis Model to determine the relative costs in both states. *See e.g., KS/OK 271 Order* ¶¶ 82-89; *PA 271 Order* ¶¶ 62-66; *Rhode Island 271 Order* ¶¶ 37-58. In the final determination, if the Commission determines that the non-loop rates satisfy a benchmark comparison in the aggregate, then the Commission will presume that each of the individual network elements within this group satisfy the benchmark comparison individually. *Rhode Island 271 Order* ¶ 40; *New Jersey 271 Order* ¶ 52.

A. Verizon's West Virginia Switching Rates Greatly Exceed Those Of New York On A Cost Adjusted Basis.

6. Verizon's switching rates in West Virginia fail to benchmark with the corresponding rates in New York—and fail by the widest margin of any state in Verizon's entire southern territory. This fact can be demonstrated readily by performing a benchmarking comparison that excludes transport. Such a comparison shows that Verizon's switching rates for West Virginia are 30 percent higher than the switching rates in New York on a cost adjusted basis. These results are displayed in Table 1 below:

Table 1

Cost Adjusted Switching Rates

State	UNE Switch Rate, per line per month	% Diff in UNE Switch Rate: Other states vs. NY	FCC SynMod Switch cost per line.	% Diff in SynMod UNE Switch Cost: Other states vs. NY	% Diff in Cost Adjusted UNE Switch Rate: Other states vs. NY	Implied Benchmark Rate	Rate Change Required to Benchmark
NY	$ 5.29	0%	$ 3.26	0%	0%	$ 5.29	$ -
WV	$ 7.73	46%	$ 3.67	12%	30%	$ 5.94	$ (1.79)

B. The Large Difference In Population And Line Density Between New York And West Virginia Renders Meaningless An Aggregate Benchmark Comparison Of All Non-Loop UNE Prices.

7. In several of Verizon's previous Section 271 applications, the Commission has chosen to approve Verizon's UNE prices, despite the failure of Verizon's switching prices to benchmark with New York, on the ground that Verizon's non-loop prices benchmarked with New York in the aggregate. For West Virginia, however, the enormous difference in population and line density between that state and New York renders any such comparison meaningless. Further, the magnitude of the error and penalty to CLECs is much more exaggerated in the West Virginia case, being almost five times as great as for Virginia.

8. The Synthesis Cost Model substantially overstates transport costs in states with low population density relative to states that are more densely populated. Although not all of the reasons are known, at least some of the underlying causes are evident, however. For example, even in a state where the population density is low, such as West Virginia, the Synthesis Cost Model nevertheless places OC-48 transport rings in virtually all cases. Such a network design might be appropriate for an area with high population density and a corresponding high volume

of inter-office transport traffic, such as New York, but in a rural area this configuration causes the Synthesis Cost Model to overbuild the transport network.

9. Moreover, this flaw in the Synthesis Cost Model is compounded by the default inputs that the Commission uses in the model related to interoffice costs for non-rural areas. The Commission uses the same inputs for both high density and low density areas, without making any distinction for differences in the nature or volume of the traffic in the areas. Thus, the model assumes the same percent of inter-office traffic for both West Virginia and New York despite the real world differences in both the amount and the cost of this traffic and its corresponding facilities. As a result of these unrealistic model inputs, the differences between the two states is not reflected in the inter-office facilities that the model constructs. Because of this, the model essentially builds the same inter-office network for West Virginia as it does for New York even though the requirements in the two states are likely to differ greatly. In this way, the Synthesis Cost Model overbuilds the West Virginia network and inflates the transport costs relative to New York.

10. In the context of Section 271, this flaw is important because as the relative costs become more overstated, so do the level of non-loop *rate* differences that can arguably be justified by the forward looking costs. Due to the benchmarking process previously described, the overstated transport costs inflate the apparent costs of the whole aggregated bundle of non-loop costs, which allows unreasonably high, non-TELRIC compliant switching rates, a component of this bundle, to appear to be reasonable to the Commission when the entire non-loop bundle is within the range of reasonable TELRIC prices on a cost adjusted basis. This happens because the overstated costs of transport in West Virginia inflate the aggregate costs of the entire bundle of non-loop elements for the state. Hence, rates for the non-loop elements will

appear to benchmark with New York even though the non-loop rates in West Virginia actually have a far higher aggregate markup over cost.

11. Exhibits 1 and 2 illustrate this point graphically. I have replicated the FCC benchmark process, generating UNE rate data based on the initial generation of arbitrations during the 1997-99 period (see Exhibit 1).[1] For both switch-related and transport (nonswitching, nonloop), I calculated the ratio of SynMod cost to UNE rate (1st round arbitration). See Exhibit 2). Exhibit 2 provides the per line amounts required to calculate the ratios shown in the line plots, consistently with the Commission's methodology, for Verizon's local operating companies in Delaware, Maryland, New Jersey, New York, Pennsylvania, Virginia, and West Virginia.

12. The graph in Exhibit 2 compares the estimates of Verizon's transport costs generated by, the Synthesis model for each state in the Verizon South territory (plus New York) with the UNE prices actually set by state commissions in each state.[2] As the exhibit shows, the estimates of transport costs generated by the Synthesis Model, while roughly comparable to commission-prescribed transport prices in the higher density states, climb dramatically above the latter values in the lower density states. Because Verizon's service area in West Virginia has a

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[1] The current rates are a mixture of 1st and 2nd arbitration rounds. Given the declining cost trend of the arbitrations, reflecting the declining industry unit cost, a consistent relationship can not be established from a data set that mixes both generations of rate cases.

[2] Because UNE prices set by state commissions have trended down significantly over time, the analysis compares rates of approximately the same vintage—i.e., rates set during the 1997-99 period. In addition, to assure comparability, in computing the per-line UNE prices we assumed the same volumes as assumed in the Synthesis Model. Needless to say, AT&T does not contend that the transport UNE prices set by state commission are themselves TELRIC compliant; to the contrary, a number of those prices exceed TELRIC levels as well. Nevertheless, those prices are the best available indicator of state-specific transport costs for an analysis of this kind, and they provide a clear qualitative demonstration of the inverse relationship between line density and the overstatement of transport costs by the Synthesis Model.

much lower density of population (and thus lines) than Verizon's service area in New York, the problem squarely arises here as well.

13. This exhibit clearly shows that (1) there is a clear distortion in the relationship for transport; (2) there is no trend in the relationship between SynMod and UNE rates as it relates for switching; and (3) consequently, there is no understatement of switching costs in low density areas to offset the overstatement of transport costs in the same areas.

14. Given the magnitude of the switch benchmarking problem between West Virginia vs. New York ($1.79), the $0.51 of transport related cost per line for West Virginia (based on current rates) would have to have an underlying cost per SynMod of $1.46 (SynMod transport cost for West Virginia), a multiple of three times to be correctly reflecting reality. Put another way, the Verizon cost study that created the underlying rates would have to have been understated by this magnitude. The foregoing analysis disposes of the Commission's speculation in its Virginia 271 Decision (at 102) that the apparently inverse correlation between line density and the price level of unbundled transport "may simply reflect the fact that some states have set transport rates at the high end of the reasonable range, while other states have set transport rates at the low end." Controlled for the vintage of the rates, the inverse correlation between density and the level of transport prices is striking. If there exists some unanimous policy preference among Verizon's state regulators to require Verizon's customers to pay markups over the cost of transport that vary with inverse correlation with population density, such a policy has never been articulated by any of the regulators in question.

15. Equally unsupported is the Commission's response to the fact that the transport costs generated by the Synthesis Model in the pending Virginia arbitration were nearly *three times* the costs generated by Verizon's own model. That the Synthesis Model may not provide

an accurate measure of "absolute" transport costs, the Commission asserts, is no reason not to use it to estimate "relative cost differences" among states. Virginia 271 Decision ¶ 103. The obvious flaw in this reasoning, however, is that unless the error in the transport cost estimates is invariant with respect to density, the transport cost module cannot be relied on to estimate relative cost differences either.

16. The existence of the "extensive record" developed in the rulemaking proceeding leading to the adoption of the Synthesis Model (*Virginia 271 Decision* ¶ 104) also provides no justification for relying on the model in particular circumstances where it is demonstrably ill-suited. The purpose of the rulemaking proceeding that led to adoption of the Synthesis Model was for universal service subsidy calculations, in which relative differences in transport costs play a relatively small part.

17. Equally illogical is the proposition that an aggregate non-loop benchmark analysis must serve as an unrebuttable rule of decision in all cases because, "in the context of universal service, AT&T has supported the Synthesis Model before the Commission and before the appellate courts." *Virginia 271 Order* ¶ 104. AT&T has clearly expressed concerns that the Model provides a conservative -- indeed, overstated -- measure of the costs of transport.

18. It is Verizon, not AT&T, that is guilty of inconsistency on this issue. Less than a year ago, in the Virginia UNE arbitration that remains pending before the Commission, Verizon assailed the Synthesis Model (including its transport module) as "incapable of estimating company- and state-specific UNE rates with any accuracy."[3] The Model, Verizon added, "is not designed to model, nor can it be modified to account for, the costs of the full and robust network

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[3] *Petitions of WorldCom, Inc., Cox Virginia Telecom, Inc., & AT&T Communications*, CC Docket Nos. 00-218 and 00-251, Verizon Reply Post-Trial Brief on Cost Issues (Jan. 31, 2002) at 133.

that is the focus of UNE proceedings."[4] The "underlying platform" of the Model "prevents it from accurately measuring the forward-looking costs that Verizon VA or, for that matter, any efficient carrier, would incur in providing the full range of UNEs required by the Commission."[5] Verizon has never retracted these criticisms. Indeed, as noted above, in the Virginia UNE arbitration Verizon supports estimates of transport costs that are only *one third* as high as the estimates obtained by AT&T from the Synthesis Model.[6]

19. Nor can inflexible reliance on an aggregate non-loop benchmark analysis be justified on the theory that the Synthesis Model is "the best tool we have for evaluating cost differences between states." *Virginia 271 Decision* ¶ 104. When the Commission has the alternatives of (1) using the Synthesis Model to perform a comparison of the *switching*-only costs, and (2) considering the record evidence that bears directly on whether Verizon's switching rates in Virginia are TELRIC-compliant, mechanical application of the Synthesis Model to compare all non-loop costs in the aggregate is clearly *not* the best available tool in the particular circumstances here.

20. The Commission's observation that "re-examination of the Synthesis Model is an immensely complicated inquiry not suited to the section 271 process" (Virginia 271 Order ¶ 105) also misses the point. *Redesigning* the Synthesis Model to eliminate its tendency to overstate transport costs is certainly beyond the scope of a 271 proceeding. But *recognizing* that the Model suffers from error in the particular circumstances of this case, and *reconsidering* whether an aggregate non-loop benchmark should remain the conclusive test of TELRIC compliance in

[4] *Id*.

[5] *Id*. at 134.

[6] New Hampshire/Delaware 271 proceeding, AT&T Reply Comments (Aug. 12, 2002), Lieberman/Pitkin Reply Decl. ¶¶ 18-19.

these circumstances, are at the core of the Commission's duties within this case. Section 271 requires the Commission to decide whether Verizon's UNE prices in Virginia are just and reasonable—and to make that decision based on the best evidence available within the 90 day statutory life of this case, not some future proceeding. Because the Synthesis Model does not estimate relative transport costs accurately, the best available evidence of rate reasonableness in this proceeding are (1) benchmark analyses that exclude transport, and (2) direct scrutiny of the TELRIC compliance of Verizon's rates. This declaration, and the accompanying declaration of Michael Baranowski, demonstrate that Verizon's switching prices in West Virginia flunk both tests.

21. The Commission's suggestion that separate benchmarking of switching rates would "promote form over substance" because CLECs do not currently buy unbundled switching separately from unbundled transport and other non-loop elements (*Virginia 271 Order* ¶¶ 110-112) ignores the reality that the density-related overstatement of transport costs by the Synthesis Model overstates the *aggregate* costs of non-loop elements in the lower density states, and therefore understates their *aggregate* rate-to-cost ratios. The flaw in the transport module of the Synthesis Model—a tendency to overstate transport costs, and to overstate them more in states with lower population density—exaggerates relative costs in lower density states, and understates their cost-adjusted rates, for the non-loop elements in the aggregate, *not just transport alone*. A benchmark analysis of aggregate nonloop costs that relies on Synthesis Model data on the cost differences vis-à-vis New York allows Verizon to inflate the cost of competitive entry in states with lower population densities *even for CLECs that never buy switching separately from the other nonloop elements*. CLECs thus are aggrieved by this error regardless of whether they ever buy any unbundled switching separately from other non-loop elements.

22. The Commission's speculation that "benchmarking non-loop elements in the aggregate may be useful to help account for rate structure differences between states" (Virginia 271 Order ¶ 112) is also unfounded. The Commission's apparent assumption is that differences exist among states in the recovery of costs that are incurred by "other non-loop" elements (such as shared trunk ports and signaling) in common with switching usage. The benchmark analysis sponsored in this declaration, however, includes the revenues and costs of those elements as well within the switching bucket.

III. CONCLUSION

23. Based on my analysis, it is clear that Verizon's West Virginia switching rates fail to benchmark with New York. Moreover, the apparent benchmarking of Verizon's *aggregate* nonloop rates in West Virginia with New York is an illusion created by the relative overstatement of transport costs by the Synthesis Model in West Virginia compared with New York.

VERIFICATION PAGE

I declare under penalty of perjury that the foregoing Declaration is true and correct.

/s/ Michael Lieberman

Michael Lieberman

Executed on: January 9, 2003